Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554

In the Matter of	
Petition of U S WEST Communications, Inc. for Waiver or Alternative Relief To Permit Adjustment to Access Charge Tariff	CC Docket No. 97-250 CCB/CPD No. 98-32

REPLY OF U S WEST COMMUNICATIONS, INC.

William T. Lake
John H. Harwood II
David M. Sohn
Wilmer, Cutler & Pickering
2445 M Street, NW
Washington, DC 20037-1420
202-663-6000

Robert B. McKenna
U S WEST, Inc.
Suite 700
1020 19th Street, NW
Washington, DC 20036
303-672-2799

Counsel for U S WEST Communications, Inc.

Dan L. Poole, of Counsel

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SUMMARY

The oppositions of AT&T and MCI offer no persuasive reason to deny the petition of U S WEST Communications, Inc. ("USWC") for waiver or alternative relief. The petition satisfies the legal standards for the relief it requests. The underrecovery that USWC seeks to remedy clearly was "triggered by" the complex shift to a new access charge structure, and the contrary claims of AT&T and MCI are based on an untenably narrow view of causation. USWC likewise has demonstrated unique hardship: Of the various errors that undoubtedly were made in implementing the restructuring of access charges, only USWC had the misfortune of making an error with such large financial consequences. And granting the petition would not constitute retroactive ratemaking. USWC does not seek to change the terms of past transactions; rather, it asks the Commission to consider certain past events—namely, the extraordinary regulatory transition and the disruption it caused to USWC's rates—as antecedent facts that are relevant to the determination of an equitable prospective rate.

The other legal arguments of AT&T and MCI are similarly unconvincing, and neither carrier makes a serious attempt to show that denying the petition would produce a just result. By contrast, the relief USWC has requested would produce a sensible and equitable outcome. Accordingly, the Commission should reject the arguments of AT&T and MCI and grant USWC's petition.

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U S WEST Communications, Inc. ("USWC"), pursuant to the Commission's Public Notice of April 24, 1998, submits this reply to the oppositions of AT&T and MCI to USWC's April 22, 1998 petition for waiver or alternative relief.

As described in USWC's petition, an unintended loophole created in the course of access charge reform will, absent remedial action by the Commission, result in a severe and undeserved financial detriment for USWC and a large, unjustified bonus for access customers such as AT&T and MCI. USWC emphasized that the circumstances are extraordinary in at least two respects: The loophole was a byproduct of a revolutionary shift in the regulatory regime, and it produced financial consequences simply too large to shrug off. USWC accordingly proposed remedial action that would be legally appropriate and would produce a sensible and equitable outcome.

AT&T and MCI, naturally reluctant to relinquish their unearned financial benefit, present a number of narrow legal arguments that sidestep rather than confront the special

equitable considerations presented by USWC's petition. But their legal arguments cannot withstand scrutiny:

- AT&T and MCI deny that the radical shift in the regulatory regime "triggered" the costs from which USWC seeks relief, as the legal standard for exogenous treatment requires. But ignoring the key role played by the regulatory shift simply because other factors also played a role defies the common sense notion of causation.

- AT&T and MCI claim that USWC has not shown any "special circumstances," as required by the legal standard for waiver—even though USWC plainly demonstrated a $30 million detriment that applies uniquely to it.

- AT&T and MCI assert that USWC's proposed relief would constitute retroactive ratemaking—deliberately disregarding the crucial legal distinction between changing the terms of past transactions and using relevant antecedent facts in setting appropriate terms for future transactions.

- AT&T and MCI wrongly suggest that, in order to make USWC's proposed adjustment to future rates, the Commission would have to have given advance notice in the proceeding concerning the propriety of current rates.

Moreover, neither AT&T nor MCI makes a serious attempt to show that denying the petition and cementing the loophole's essentially random financial consequences would produce a just result. The Commission should therefore reject their arguments and grant USWC's petition.

I. USWC's Petition Satisfies the Threshold Legal Standards for the Relief It Requests.

AT&T and MCI attempt to short-circuit meaningful consideration of USWC's petition by claiming that the petition fails to satisfy the formal legal standards for the relief it requests. AT&T, quoting the Commission's statement that exogenous costs are "in general those costs that are triggered by administrative, legislative or judicial action beyond the control of the carriers," argues that the harm from which USWC seeks relief was within its own control and

therefore cannot be treated as an exogenous cost.[1/] But the very essence of USWC's claim is that the costs at issue here were in fact "triggered by" administrative action—the complex restructuring of access charges—beyond USWC's control. As USWC demonstrated in its petition, the extraordinary nature of the regulatory change made it all but inevitable that there would be at least some pitfalls in making the transition. Indeed, the Commission itself acknowledged the "unusual circumstances" involved in the "massive restructuring of many interrelated rates," and concluded that the special difficulties involved in complying with such an extensive reform might warrant the unusual step of "allowing LECs some measure of recoupment" for undercharges.[2/] This reflects a recognition that, in this difficult transitional environment, there was no practical way of eliminating the possibility of errors in rate calculations.

USWC's underrecovery was no less "triggered by administrative . . . action" because the mandated rate restructuring did not make USWC's particular underrecovery costs strictly inevitable when considered with the benefit of hindsight. If an automobile hits a tree after swerving to avoid a deer, one would have no difficulty saying that the accident was "triggered by" the deer, even if later examination of the accident scene reveals that the driver might have avoided damage by swerving left instead of right. The driver may have contributed to the accident, and other drivers in the same position might not have had the same accident, but there would be no question that the accident was triggered by an event outside the driver's

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1/ AT&T Opp. at 3-4.

2/ Tariffs Implementing Access Charge Reform, Memorandum Opinion and Order, DA 97-2724 (rel. Dec. 30, 1997) ("Access Reform Tariff Investigation Order") ¶ 7.

control.[3/]

The legal standard for exogenous adjustments does not require a narrower conception of causation than the accident example discussed above. Rarely will the costs associated with an administrative, legislative, or judicial decision be strictly inevitable; in hindsight, it will almost always be possible to identify actions that a carrier could have taken in advance to minimize the impact of the action. But carriers do not have the benefit of hindsight, and the Commission has never stated that it will limit exogenous adjustments to those costs that even in hindsight appear to have been strictly inevitable.

AT&T and MCI also argue that USWC has not demonstrated "special circumstances" and therefore has not satisfied the legal standard for a waiver. MCI bases this claim on the same, flawed causation argument discussed immediately above,[4/] ignoring that the underrecovery was directly traceable to the complexity of the restructuring. AT&T similarly misses the point, arguing there is no unique hardship or burden because "[a]ll price cap LECs

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[3/] AT&T repeatedly quotes the petition's observation that the flaw that caused the undercharges was in essence "a random mathematical mistake," as if this statement represents some kind of concession. AT&T Opp. at 3-4, 6. AT&T simply misses the point. Given the complexity of the restructuring, it was virtually inevitable that some calculation mistakes would occur. But the particular mistakes, as well as the extent of their financial impact, were essentially random—USWC could just as easily have made a different and less costly mistake instead of the one it actually made, and other carriers could have made serious mistakes just as easily as USWC. That does not mean the mistakes that did occur were not direct byproducts of the restructuring.

[4/] MCI Opp. at 7 (asserting that USWC's underrecovery "cannot be blamed" on the access reform proceeding).

went through the same regulatory changes that U S WEST did."[5/] While all carriers went through the regulatory change, only USWC suffered a $30 million detriment as a result. USWC's core argument is that this could have happened to any of the carriers, because errors were inevitable given the complexity of the change. USWC's unique hardship is that, of the various errors that were undoubtedly made in implementing the restructuring, only USWC had the misfortune of making an error with such tremendous financial consequences.

AT&T also is wrong when it disputes USWC's claim that the waiver granted to NYNEX in 1995 is analogous to the relief requested here by USWC.[6/] As USWC explained in its petition, there are critical similarities between the two cases. In the NYNEX case, as here, appropriate action by the carrier to adjust to the regulatory decision could have avoided the loss; the regulatory decision did not make the loss inevitable. The Commission granted a waiver nonetheless, on the ground that doing so would produce financial results consistent with both the agency's intended policy and the parties' expectations.[7/] Contrary to AT&T, the analogy to the present case is clear.

5/ AT&T Opp. at 5.

6/ See AT&T Opp. at 5-6; Pet. at 16-17. AT&T observes that the NYNEX waiver request did not "involve the petitioning company calculating incorrect rates as a result of an oversight." AT&T Opp. at 6.

7/ See Pet. at 17; NYNEX Telephone Companies 1995 Annual Access Tariff Filings, Requests for Waiver, 11 FCC Rcd. 5448 (1995).

II. Considering Antecedent Facts in Setting Forward-Looking Rates, as USWC Has Asked the Commission To Do, Does Not Constitute Unlawful Retroactive Ratemaking.

USWC demonstrated in its petition that the relief it seeks would not violate the prohibition against retroactive ratemaking.[8/] USWC is not seeking to change the legal consequences of past access service transactions: Its proposed tariff adjustment would affect future rates only, and the amounts paid by those who purchased access services during the first three months of 1998, based strictly on the rates in effect at the time, will not change. Nobody will be rebilled or otherwise asked to incur any additional liability for the transactions they entered into during those months.

AT&T and MCI nonetheless contend that the relief USWC requests would constitute retroactive ratemaking, quoting from decisions stating that the retroactive ratemaking doctrine bars the Commission from allowing a carrier to raise rates to recoup past underrecovery.[9/] But the force of these decisions is substantially limited by cases to the effect that a rule "is not made retroactive merely because it draws on antecedent facts for its operation."[10/] Ignoring these cases, AT&T and MCI argue for a simplistic and one-sided approach to the retroactivity issue that would strictly prohibit the Commission from considering antecedent facts in regulating future rates—at least where those facts tend to support a higher

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8/ Pet. at 18-25.

9/ AT&T Opp. at 6-7; MCI Opp. at 2-3.

10/ Landgraf v. USI Film Products, 511 U.S. 244, 270 n.24 (1994) (quoting Cox v. Hart, 260 U.S. 427, 435 (1922)); see also Bell Atlantic Telephone Cos. v. FCC, 79 F.3d 1195, 1207 (D.C. Cir. 1996).

future rate. As the Supreme Court has stated, and as USWC pointed out in its petition, retroactivity analysis is neither so simple nor so narrowly constrained: "Any test of retroactivity will leave room for disagreement in hard cases . . . However, retroactivity is a matter on which judges tend to have sound instincts, and familiar considerations of fair notice, reasonable reliance, and settled expectations offer sound guidance."[11/]

The proper reading of the cases AT&T and MCI cite is that the past failure of a carrier to recover the full amount permitted by the regulatory regime does not by itself justify an increase in future rates. At the same time, there is no legal bar to permitting such an increase where antecedent facts create special equitable considerations. The retroactive ratemaking doctrine does not eliminate the Commission's discretion to consider past events that have a bearing on the reasonableness of prospective rates.[12/]

The cases USWC cited in the petition make this clear. In New England Telephone and Telegraph Co. v. FCC, the D.C. Circuit upheld a Commission order reducing future rates "to compensate for past surpluses" in the carriers' earnings.[13/] The court held that the rate adjustment was a reasonable way to remedy past earnings in excess of the rate-of-return prescription, and thus fell within the scope of the Commission's general discretion to take remedial action in matters within its regulatory purview. In Town of Norwood, Massachusetts v.

11/ Landgraf, 511 U.S. at 270 (internal quotations and citations omitted); see Pet. at 19.

12/ By the same token, if the retroactive ratemaking doctrine limited the Commission's power in the manner described by AT&T and MCI, the Commission also would be barred from taking action to reduce prospective rates based on consideration of past events.

13/ 826 F.2d 1101, 1107 (D.C. Cir. 1987); see Pet. at 20-21.

FERC, the D.C. Circuit upheld the FERC's decision to allow a prospective rate increase designed to recoup special costs associated with the transition to a new regulatory rule.[14/] And in Bell Atlantic Telephone Cos. v. FCC, the court approved the Commission's "sharing" mechanism, which required a carrier to reduce rates in one year by an amount equal to the carrier's overearnings in the prior year.[15/] In each of these cases, the adjustment to future rates produced results that were equitable and consistent with the aims of the regulatory regime. Thus, where special equitable considerations apply, the retroactive ratemaking doctrine does not bar the Commission from factoring them in to future rates.

MCI's efforts to dismiss the relevance of these cases are unsuccessful. For example, MCI argues that the sharing mechanism upheld in Bell Atlantic differs from USWC's requested relief because sharing "use[s] past earnings as an indicator of the rates that would be just and reasonable for the future."[16/] But so would USWC's requested relief: USWC's petition asks the Commission simply to treat the extraordinary regulatory transition and the disruption it has caused to USWC's rates and earnings as antecedent facts that have substantial bearing on what constitutes an equitable forward-looking rate.

MCI also points to language in Town of Norwood stating that a utility cannot adjust future rates to recoup losses caused by errors in the utility's economic projections.[17/] But the court in Norwood clearly held that the situation is different where the shortfall concerns

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14/ 53 F.3d 377 (D.C. Cir. 1995); see Pet. at 21-22.

15/ 79 F.3d 1195 (D.C. Cir. 1996); see Pet. at 21.

16/ MCI Opp. at 3.

17/ MCI Opp. at 4.

amounts that all parties originally expected the utility to collect. Indeed, the key holding of that case was that, where a regulatory transition inadvertently caused an unexpected shortfall in a utility's recovery as a result of what was essentially an accounting discrepancy, the regulatory agency could permit the utility to increase its future rates to make up the shortfall. In other words, underrecovery that occurs in the ordinary operation of the regulatory regime as a result of the inherently imprecise nature of economic and business forecasting is entirely different from one-time underrecovery problems related to a major regulatory transition. The present case, like Town of Norwood, involves a one-time transition problem.

III. USWC's Proposed Relief Would Not Disturb Any Settled Expectations of Its Access Customers.

As USWC explained in its petition, the Commission, access providers, and access customers all expected that the restructuring of access charges would be revenue neutral. USWC's access customers may have been pleasantly surprised when they later discovered a reduction in their bills, but they also knew not to rely on the new rates, because the Access Reform Tariff Investigation Order put them on notice that the rates were provisional and hence subject to change. Indeed, the investigation had the potential to change virtually every rate in the filing, because it covered a broad range of issues that could result in changes to price cap indices and service band indices in every price cap basket. Thus, nobody could have had a substantial reliance interest in any particular future rate.

AT&T and MCI make much of the fact that the Access Reform Tariff Investigation Order does not expressly contemplate the precise type of adjustment proposed by

USWC.[18] MCI also argues that, whatever customers may have expected to pay before the restructuring, once new rates were filed, the customers would have expected to pay only the filed rate.[19] These arguments again miss the point. Advance notice would be essential if USWC was proposing to go back and rebill access customers based on services used in the first three months of 1998.[20] But USWC's petition does not seek to revisit prices for services sold from January to March; bills for such services would be unaffected by its proposed relief. Rather, as noted above, USWC seeks to make an adjustment to future rates—specifically, rates for access services purchased in the second half of 1998. Thus, express advance notice is not a prerequisite to USWC's proposed adjustment.

Of course, expectations are highly relevant in determining whether USWC's proposed remedy is equitable. But given the expectation of revenue-neutrality and the provisional nature of the initial rates, no access customer could have reasonably expected that the restructuring of access charges would give him an entitlement to a quick financial bonus. USWC's proposal would simply put all parties in the same financial position they anticipated when the restructuring process began.

18/ See AT&T Opp. at 7; MCI Opp. at 6.

19/ MCI Opp. at 5.

20/ That is why the Access Reform Tariff Investigation Order provided express advance notice of a possible "two-way adjustment"; it effectively was warning customers that the price paid for a service used in January could be revisited and might be subject to a subsequent adjustment.

IV. USWC's Proposed Adjustment Would Produce an Equitable Outcome.

The Commission might be justified in overlooking restructuring mistakes that have relatively little financial impact; small mistakes may well cancel each other out and in any event do not raise major fairness concerns. Indeed, USWC has not requested relief from the effect of a lesser flaw in its tariff.[21/] But here, where the financial impact is particularly large, remedial action is warranted. Without such action, a restructuring intended and expected to be revenue neutral will have the effect of taking $30 million from USWC and giving it to access service customers such as AT&T and MCI. AT&T and MCI cannot show that such an outcome is sensible, just, or in the public interest. There is no evidence, for example, that they have passed on this unearned bonus to consumers in the form of lower long distance rates. In short, what is at stake here is an inadvertent and unearned company-to-company transfer of $30 million. Regulatory action created the circumstances that led to the transfer, and regulatory action is needed to provide a remedy.

AT&T briefly suggests that equity requires the denial of USWC's petition, on the theory that "had U S WEST erroneously inflated its TIC rate and had its tariff taken effect without suspension or investigation, the access customer would not be permitted to recoup the

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21/ USWC used the Commission's form for calculating new access rates, which incorrectly assumed that USWC determines end user common line rates on a company-wide rather than a state-by-state basis. This discrepancy ultimately resulted in a lower access rate calculation, but the effect was minor relative to the miscalculation at issue in this proceeding. USWC corrected the discrepancy in its March 1998 tariff filing and does not plan to seek relief from the financial effects the discrepancy caused prior to the correction.

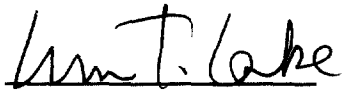
overcharges."[22] But the USWC tariff at issue here did not "take[] effect without suspension or investigation;" on the contrary, it was subject to a suspension and investigation order. Thus, AT&T's argument is simply not relevant. If USWC had overcharged customers by a substantial amount—for example, $30 million—the Commission almost certainly would have elected to take remedial action. For treatment to be symmetrical, therefore, the Commission would have to be willing, under appropriate circumstances, to take remedial action with respect to large and unintended undercharges as well. Thus, while AT&T is correct that symmetry of treatment is an important equitable concern, that concern actually supports a grant of USWC's petition, not a denial.

22/ AT&T Opp. at 8 (emphasis omitted).

CONCLUSION

For the reasons set forth above, and for the reasons set forth in its April 22, 1998 petition for waiver or alternative relief, the Commission should grant the relief USWC has requested.

Respectfully submitted,



William T. Lake
John H. Harwood II
David M. Sohn
Wilmer, Cutler & Pickering
2445 M Street, NW
Washington, DC 20037-1420
202-663-6000

Robert B. McKenna
U S WEST, Inc.
Suite 700
1020 19th Street, NW
Washington, DC 20036
303-672-2861

Counsel for U S WEST Communications, Inc.

Dan L. Poole, Of Counsel

June 10, 1998

CERTIFICATE OF SERVICE

I, Rebecca Ward, do hereby certify that on this 10th day of June, 1998, I have caused a copy of the foregoing **REPLY OF U S WEST COMMUNICATIONS, INC.** to be served, via first class United States Mail, postage pre-paid, upon the persons listed on the attached service list.

Rebecca Ward

Rebecca Ward

*Served via hand-delivery

*William E. Kennard
Federal Communications Commission
Room 814
1919 M Street, N.W.
Washington, DC 20554

*Gloria Tristani
Federal Communications Commission
Room 826
1919 M Street, N.W.
Washington, DC 20554

*Michael K. Powell
Federal Communications Commission
Room 844
1919 M Street, N.W.
Washington, DC 20554

*Harold Furchtgott-Roth
Federal Communications Commission
Room 802
1919 M Street, N.W.
Washington, DC 20554

*Susan P. Ness
Federal Communications Commission
Room 832
1919 M Street, N.W.
Washington, DC 20554

*Kathryn C. Brown
Federal Communications Commission
Room 500
1919 M Street, N.W.
Washington, DC 20554

*Jane E. Jackson
Federal Communications Commission
Room 518
1919 M Street, N. W.
Washington, DC 20554

*Judith A. Nitsche
Federal Communications Commission
Room 518
1919 M Street, N.W.
Washington, DC 20554

*Yvonne Hawkins
Federal Communications Commission
Room 518
1919 M Street, N.W.
Washington, DC 20554

*International Transcription
Services, Inc.
1231 20th Street, N.W.
Washington, DC 20036

Alan Buzacott
MCI Telecommunications Corporation
1801 Pennsylvania Avenue, N.W.
Washington, DC 20006

Gail L. Polivy
GTE Service Corporation
Suite 1200
1850 M Street, N.W.
Washington, DC 20036

R. D. Boswell
BellSouth Telecommunications, Inc.
675 Peachtree Street, N.E.
Atlanta, GA 30375

Robert M. Lynch
Durward D. Dupre
Southwestern Bell Telephone
Company, *et al.*
Room 2403
One Bell Plaza
Dallas, TX 75202

Jay C. Keithley
Sprint Communications Company, Inc.
11th Floor
1850 M Street, N.W.
Washington, DC 20036-5807

M. Robert Sutherland
Richard M. Sbaratta
Rebecca M. Lough
BellSouth Telecommunications, Inc.
Suite 1700
1155 Peachtree Street, N.E.
Atlanta, GA 30309-3610

Edward Shakin
Edward D. Young III
Michael E. Glover
Bell Atlantic Telephone Companies
8th Floor
1310 North Court House Road
Arlington, VA 22201

Wendy Blueming
Southern New England Telephone
Company
227 Church Street
New Haven, CT 06510

Nancy C. Woolf
Pacific Bell and Nevada Bell
Room 1529
140 New Montgomery Street
San Francisco, CA 94105

Michael S. Pabian
Ameritech
Room 4H82
2000 West Ameritech Center Drive
Hoffman Estates, IL 60196-1025

Michael J. Shortley III
Frontier Telephone Companies
180 South Clinton Avenue
Rochester, NY 14646

Robert A. Mazer ALIANT
Albert Shuldiner
Allison Yamamoto Kohn
Vinson & Elkins, LLP
1455 Pennsylvania Avenue, N.W.
Washington, DC 20004-1008

Christine Jines
SBC Communications Inc.
Suite 1100
1401 I Street, N.W.
Washington, DC 20005

Nancy Wind
SBC Communications Inc.
Room 7-W-7
One Bell Center
St. Louis, MO 63101

Nancy Rue CBTC
Frost & Jacobs
2500 Central Trust Center
201 East 5th Street
Cincinnati, OH 45202

Maureen Kennan
Bell Atlantic Telephone Companies
NYNEX
10th Floor
2980 Fairview Park Drive
Falls Church, VA 22042

Jacob J. Goldberg
NYNEX
Suite 400 West
1300 I Street, N.W.
Washington, DC 20005

Thomas E. Taylor
Cincinnati Bell Telephone Company
6th Floor
201 East 4th Street
Cincinnati, OH 45202

Richard M. Tettelbaum
Citizens Telecommunications Companies
Suite 500
1400 16th Street, N.W.
Washington, DC 20036

Sandra K. Williams
Sprint Corporation
POB 11315
Kansas City, MO 64112

Mark C. Rosenblum
Peter Jacoby
Judy Sello
AT&T Corp.
Room 3245I1
295 North Maple Avenue
Basking Ridge, NJ 07920

Gene C. Schaerr
James P. Young
Rudolph M. Kammerer
Carl D. Wasserman
Sidley & Austin
1722 Eye Street, N.W.
Washington, DC 20006

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